

Message Text

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ACTION EB-08

INFO OCT-01 AF-10 ARA-10 EUR-12 EA-10 NEA-10 ISO-00
SOE-02 AID-05 CEA-01 CIAE-00 COME-00 DODE-00
DOE-11 H-01 INR-07 INT-05 L-03 NSAE-00 NSC-05
OMB-01 PM-05 USIA-06 OES-07 SP-02 SS-15 STR-06
TRSE-00 ACDA-12 PA-01 PRS-01 /157 W
-----007514 131719Z/45

R 131522Z JAN 78
FM AMEMBASSY LAGOS
TO SECSTATE WASHDC 5897
INFO AMCONSUL IBADAN
AMCONSUL KADUNA
AMEMBASSY ABU DHABI
AMEMBASSY ALGIERS
USINT BAGHDAD
AMEMBASSY DOHA
AMCONSUL DHAHRAN
AMEMBASSY JAKARTA
AMEMBASSY JIDDA
AMEMBASSY KUWAIT
AMEMBASSY LIBREVILLE
AMEMBASSY LONDON
AMEMBASSY QUITO
AMEMBASSY TEHRAN
AMEMBASSY TRIOPOLI
AMEMBASSY VIENNA

LIMITED OFFICIAL USE SECTION 1 OF 2 LAGOS 0538

E.O. 11652: N/A
TAGS: ENRG, EINV, NI
SUBJECT: TEXACO/CHEVRON SIGN PARTICIPATION AGREEMENT WITH NIGERIA

1. TEXACO AND CHEVRON SIGNED PARTICIPATION AGREEMENT WITH NIGERIAN NATIONAL PETROLEUM CORPORATION (NNPC) ON JANUARY 6 GIVING NNPC
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55 PERCENT INTEREST IN OIL EXPLORATION AND PRODUCTION OPERATIONS OF TWO COMPANIES IN NIGERIA. TEXACO AND CHVRON, WHO NOW EACH HAVE 22.5 PERCENT INTEREST, RECEIVED DOLLARS 65.9 MILLION FOR ASSETS AND DOLLARS 5.7 MILLION FOR WORKING CAPITAL ACQUIRED BY NNPC. AGREEMENT IS RETROACTIVE TO MAY 1975. COMPANIES WILL HAVE NO TROUBLE COLLECTING THEIR MONEY SINCE THEY HAVE IN EFFECT BEEN LIFTING NNPC'S OIL SINCE MAY 1975 WITHOUT TURNING FUNDS OVER

TO GOVERNMENT.

2. THE BASIS FOR COMPENSATION IN THIS AGREEMENT WAS NET BOOK VALUE FOR THE ENTIRE 55 PERCENT. THIS HAS PARTICULAR SIGNIFICANCE AT THIS TIME BECAUSE THE NNPC HAS RECENTLY SAID IT WISHES TO REOPEN COMPENSATION NEGOTIATIONS WITH GULF, MOBIL AND AGIP-PHILLIPS. THESE FIRMS WERE PAID IN FULL IN NOVEMBER 1976 ON THE BASIS OF UPDATED BOOK VALUE FOR THE FIRST 35 PERCENT, AND NET BOOK VALUE FOR THE REMAINING 20 PERCENT. THE NNPC HAS INDICATED IT WANTS COMPENSATION FOR THE ENTIRE 55 PERCENT TO BE BASED ON NET BOOK VALUE, AS WAS APPARENTLY THE CASE IN COMPENSATION AGREEMENTS WORKED OUT WITH PERSIAN GULF STATES. THE COMPANIES HAVE OBJECTED THAT THIS WOULD NOT ONLY RENDER AGREEMENTS WITH THE NNPC MEANINGLESS, BUT WOULD ALSO INVOLVE RETURNING HALF THE COMPENSATION RECEIVED TO THE FMG. THIS WOULD EFFECTIVELY NULLIFY THE BENEFITS OF THE NEW PETROLEUM INVESTMENT INCENTIVES ANNOUNCED LAST MAY AND SEVERAL COMPANIES HAVE THREATENED TO CANCEL THEIR PLANS FOR MASSIVE NEW FIVE YEAR EXPLORATION, DRILLING AND DEVELOPMENT PROGRAMS IF THE NNPC INSISTS ON REOPENING THE COMPENSATION ISSUE. HOWEVER, WITH THE TEXACO/CHEVRON NET BOOK VALUE SETTLEMENT UNDER ITS BELT, THE NNPC IS SURE TO TAKE A TOUGHER NEGOTIATING POSITION WITH THE OTHER COMPANIES.

2. ONE SIGNIFICANT MITIGATING FACTOR IS THAT THE DEFINITION OF NET BOOK VALUE IN THE TEXACO/CHEVRON AGREEMENT IS NOT THE CLASSICAL

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NNN

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ONE USED IN U.S. ACCOUNTING PRACTICES INVOLVING REDUCTION OF ASSET VALUE BY DEPRECIATION. THE NIGERIAN PETROLEUM PROFITS TAX ORDINANCE DOES NOT PERMIT DEDUCTION OF BOOK DEPRECIATION FROM INCOME TAXES, BUT INSTEAD PERMITS DEDUCTION OF VARIOUS CAPITAL ALLOWANCES WHICH REDUCE TAXES BY SUBSTANTIALLY LESS THAN WOULD NORMAL CAPITAL DEPRECIATION. THUS, THE NET ASSET VALUE ARRIVED LIMITED OFFICIAL USE

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AT FOR COMPENSATION IS HIGHER THAN WOULD BE THE CASE UNER TRADITIONAL NET BOOK VALUE CALCULATION. ACCORDING TO SOURCES, THE NNPC IS USING WHAT WOULD BE TERMED TAX NET BOOK VALUE IN U.S. NEVERTHELESS, THIS STILL PLACES A LOWER VALUE ON OIL COMPANY ASSETS THAN UPDATED BOOK VALUE, WHICH ADJUSTS NET BOOK VALUE UPWARD BY WHAT IS KNOWN AS THE MIDDLE-EAST CONSTRUCTION PRICE FORMULA. IN THE CASE OF ONE OF THE OTHER U.S. OIL COMPANIES, TAX NET BOOK VALUE AS USED IN THE TEXACO/CHEVRON AGREEMENT WOULD GIVE THEM DOLLARS 24 MILLION LESS THAN UPDATED BOOK VALUE. THIS IS NOT AS BAD AS NET BOOK VALUATION, WHICH WOULD YIELD THEM DOLLARS 44 MILLION LESS THAN UPDATED BOOK VALUATION, BUT IT ST WL REPRESENTS A CONSIDERABLE REDUCTION IN THEIR COMPENSATION.

3. ONE ARGUMENT WHICH GULF, MOBIL AND AGIP-PHILLIPZDBILL USE IN RESISTING NNPC EFFORTS TO RENEGOTIATE THEIR COMPENSATION IS THAT THE TEXACO/CHEVRON AGREEMENT, WHICH IS EFFECTIVE AS OF MAY 1975, SHOULD HAVE NO EX POST FACTO LEGAL IMPACT ON THEIR OWN AGREEMENTS, WHICH WERE EFFECTIVE APRIL 1974. IT IS DOUBTFUL THAT THE NNPC WILL HEED SUCH LEGAL NICETIES. ON THE OTHER HAND, THE BARGAINING POSITION OF THE OTHER COMPANIES IS STRONGER NOW THAN IT WOULD HAVE BEEN A YEAR AGO BECAUSE DEMAND FOR NIGERIAN OIL IS

WEAKER, ALTERNLZIVE OIL FROM THE NORTH SEA AND ALASKA IS AVAILABLE, AND REFINERIES ARE INCREASINGLY ABLE TO PROCESS SOUR CRUDES FROM THE GULF. MOREOVER, NIGERIA IS SHORT OF REVENUE AND CAN ILL AFFORD TO LET A DISPUTE OVER A FEW TENS OF MILLIONS OF DOLLARS JEOPARDIZE ITS HOPES FOR DEVELOPING MAJOR NEW RE-SERVES AND INCREASING OR EVEN MAINTAINING OIL PRODUCTION LEVELS AND REVENUES OVER THE NEXT FIVE YEARS.

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